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C O N F I D E N T I A L SECTION 01 OF 04 CARACAS 000745

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SUBJECT: CHAVEZ AFTER FIVE WEEKS

CLASSIFIED BY AMBASSADOR JOHN F. MAISTO. REASON: 1.5 (D).

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SUMMARY  
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1. (C) PRESIDENT HUGO CHAVEZ'S FIRST FIVE WEEKS IN OFFICE HAVE BEEN CHARACTERIZED BY DRAMATIC AND CONFRONTATIONAL ADVANCEMENT OF HIS AGENDA OF POLITICAL AND INSTITUTIONAL CHANGE, ADMINISTRATIVE FUMBLING AS HE ATTEMPTS TO INSTALL HIS GOVERNING TEAM, AND CONTINUITY OF ECONOMIC POLICY FROM THE CALDERA ADMINISTRATION. HIS IMPATIENCE WITH ESTABLISHED PROCEDURE, PROFOUND SUSPICION OF HIS POLITICAL ADVERSARIES, AND NEED TO RESPOND TO HIS POPULAR SUPPORT BASE HAVE LED TO ACTION AND RHETORIC WHICH, WHILE WELL WITHIN THE BOUNDS OF DEMOCRATIC PRACTICE (EXCEPT FOR REMARK ABOUT THE SUPREME COURT FROM WHICH HE QUICKLY STEPPED BACK), HAVE GIVEN RISE TO CHARGES OF AUTHORITARIANISM. HIS ADVERSARIES DEEPLY RESENT HIS HECTORING WAYS, BUT HIS POPULARITY CONTINUES TO GROW WITH EACH SLASHING ATTACK AGAINST TRADITIONAL POLITICAL PARTIES AND CORRUPT PRACTICES. DURING HIS FIRST FIVE WEEKS, DEMOCRATIC INSTITUTIONS--SUCH AS THE CONGRESS AND THE SUPREME COURT--HAVE LEARNED TO PUSH BACK WHEN SHOVED, AND A RECOGNIZABLE OPPOSITION IS SLOWLY FORMING IN THE CONGRESS. IN THE MEANTIME, CHAVEZ'S GREATEST THREAT COMES NOT FROM HIS POLITICAL ENEMIES, BUT FROM AN ECONOMY WHICH CANNOT PAY THE GOVERNMENT'S BILLS, GENERATE EMPLOYMENT, OR PROVIDE THE ADDITIONAL REVENUE NECESSARY TO ADDRESS PRESSING SOCIAL NEEDS. END SUMMARY.

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THE FIRST FIVE WEEKS  
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2. (C) LIKE PECOS BILL RIDING THE TORNADO, PRESIDENT HUGO CHAVEZ HAS STRAPPED HIMSELF TO THE BACK OF VENEZUELAN DEMOCRACY AND VOWED TO RIDE IT TOWARDS PROFOUND POLITICAL AND INSTITUTIONAL CHANGE. UNDAUNTED BY ESTABLISHED PROCEDURES OR THE NICETIES OF PARLIAMENTARY DISCOURSE, THE AT TIMES RHETORICALLY AGGRESSIVE CHAVEZ HAS CHALLENGED VENEZUELA'S POLITICAL INSTITUTIONS AND ACTORS TO RESPOND TO THE RESULTS OF THE DECEMBER 6 ELECTION AND TO MAKE VENEZUELAN DEMOCRACY RELEVANT TO THE EVERY DAY CONCERNS OF THE VENEZUELAN PEOPLE.

3. (C) IN SHORT ORDER, CHAVEZ HAS:

- ISSUED A DECREE CALLING FOR A REFERENDUM ON HIS PROPOSED CONSTITUTIONAL ASSEMBLY;
- ORDERED THE NATIONAL ELECTORAL COUNCIL TO BEGIN PREPARATIONS FOR THE REFERENDUM;
- ESTABLISHED A PRESIDENTIAL COMMISSION TO LAY THE GROUNDWORK FOR SUCH AN ASSEMBLY;
- BEGUN A SERIES OF CONSULTATIONS WITH KEY SOCIAL AND POLITICAL SECTORS REGARDING THE AGENDA OF THE ASSEMBLY;
- SUBMITTED AN ECONOMIC AND FINANCIAL ENABLING LAW TO THE CONGRESS, WHICH, IF APPROVED, WOULD GIVE HIM BROAD POWERS TO

ADDRESS VENEZUELA'S FISCAL CRISIS;

-- JUMP-STARTED HIS SOCIAL AND ECONOMIC DEVELOPMENT PROGRAM THROUGH HIS "PLAN BOLIVAR 2000," A MILITARY-RUN CIVIC ACTION PROGRAM (INCLUDING SUCH WARMLY-RECEIVED WORK IN THE POOREST SECTORS OF CARACAS AS PICKING UP TRASH, PAINTING SCHOOLS, AND STAFFING CLINICS WITH MILITARY DOCTORS).

14. (C) CHAVEZ HAS PUSHED HIS AGENDA IN A PUGNACIOUS AND CONFRONTATIONAL FASHION. HE HAS LEAP-FROGGED THE CONGRESS ON THE CONSTITUTIONAL ASSEMBLY REFERENDUM, THREATENED THE SUPREME COURT WITH POPULAR WRATH THAT HE WOULD CHAMPION SHOULD IT BLOCK HIS PLANS FOR A REFERENDUM, AND CHARACTERIZED VENEZUELA'S TRADITIONAL POLITICAL PARTIES AND INSTITUTIONS AS CORRUPT AND INEFFECTIVE.

15. (C) HIS HARD-HITTING AND POPULIST RHETORIC, WHILE WITHIN THE BOUNDS OF DEMOCRATIC TRADITION AND PRACTICE, HAS PROVOKED THE RESENTMENT AND HOSTILITY OF HIS ADVERSARIES. THEIR INITIAL EFFORTS TO BLOCK OR RE-ROUTE CHAVEZ'S CONSTITUTIONAL ASSEMBLY INITIATIVE WERE STEAM-ROLLED BY CHAVEZ, WHO REFUSED TO ALLOW THEIR INSTITUTIONAL POSITION TO DILUTE OR DIMINISH WHAT CHAVEZ BELIEVES IS HIS ELECTORAL MANDATE TO EFFECT SWEEPING POLITICAL CHANGES.

16. (C) CHAVEZ'S SUCCESS IN DRIVING HIS POLITICAL AGENDA FORWARD HAS HAD ONE IMPORTANT CONSEQUENCE: MOVEMENT TOWARDS A CONSTITUTIONAL ASSEMBLY IS A REALITY. THE QUESTION NOW IS NOT WHETHER SUCH AN ASSEMBLY WILL HAPPEN, BUT HOW AND UNDER WHAT CONDITIONS. THE RECOGNITION OF THIS HAS FORCED MOST IMPORTANT POLITICAL ACTORS TO ACCEPT THE NECESSITY OF CHANGE, AND TO LOOK FOR A WAY TO LINK THEMSELVES TO THE REFORM PROCESS. AT THE SAME TIME, CHAVEZ'S CONFRONTATIONAL TACTICS HAVE ACTIVATED NATURAL DEMOCRATIC DEFENSE MECHANISMS. INSTITUTIONS, SUCH AS THE CONGRESS AND THE SUPREME COURT, ARE LEARNING HOW TO PUSH BACK WHEN SHOVED. FOR INSTANCE, WHEN CHAVEZ "THREATENED" THE SUPREME COURT ON ITS PENDING REFERENDUM DECISION, CHIEF JUSTICE CECILIA SOSA PUBLICLY LECTURED CHAVEZ ON THE SEPARATION OF POWERS AND MADE IT VERY CLEAR THAT THE COURT WOULD NOT BE INTIMIDATED. THAT MEETING WAS FOLLOWED BY A CHAVEZ VISIT TO THE SUPREME COURT, AFTER WHICH HE STATED THAT HE WOULD, OF COURSE, ACCEPT WHATEVER DECISION THE COURT MADE. THE RESULT HAS BEEN A CLEARER DEFINITION OF THE INFLUENCE AND AUTHORITY OF THESE INSTITUTIONS. ALSO, OPPOSITION TO THE GOVERNMENT IS FORMING IN THE CONGRESS AND ELSEWHERE. THIS OPPOSITION, RECOGNIZING THE NECESSITY OF CHANGE, IS WORKING TO INFLUENCE THAT CHANGE, AND ENSURE THAT IT TAKES PLACE WITHIN A DEMOCRATIC AND CONSTITUTIONAL FRAMEWORK.

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ADMINISTRATIVE FUMBLING  
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17. (C) CHAVEZ'S SUCCESS IN DRIVING FORWARD HIS POLITICAL AGENDA HAS NOT BEEN MATCHED IN THE FORMATION OF HIS GOVERNMENT. SLOW MINISTERIAL APPOINTMENTS, EVEN SLOWER SELECTION OF KEY DIRECTOR-LEVEL POSITIONS WITHIN MINISTRIES, AND THE PRESIDENT'S TENDENCY TO TALK TOO MUCH AND MAKE POLICY DURING PRESS CONFERENCES HAVE GIVEN THE FIRST MONTH OF GOVERNMENT AN AD HOC, IMPULSIVE QUALITY.

18. (C) LACKING A TESTED, LOYAL PARTY CADRE, AND FACED WITH AN ANXIOUS AND SOMETIMES INSOLENT GOVERNMENT BUREAUCRACY, CHAVEZ HAS HAD TO LOOK FOR NEW WAYS TO TAKE CONTROL OF THE MACHINERY OF GOVERNMENT. ONE WAY HAS BEEN TO NAME FORMER MILITARY OFFICERS TO KEY POSITIONS WITHIN THE BUREAUCRACY. HIS ADVERSARIES ACCUSE HIM OF "MILITARIZING" GOVERNMENT. ANOTHER INTERPRETATION WOULD BE THAT HE IS USING PEOPLE HE KNOWS AND TRUSTS TO GAIN CONTROL AND SET DIRECTION. IN SOME INSTANCES THIS STRATEGY HAS WORKED, IN OTHERS IT HAS NOT. WHILE TRUSTWORTHY, MANY OF THE MILITARY APPOINTEES HAVE NO EXPERIENCE IN CIVILIAN MINISTRIES, HAVE LITTLE POLICY ORIENTATION, AND EVEN LESS UNDERSTANDING OF THE POLITICAL NATURE OF THEIR WORK. THE RESULT HAS BEEN UNEVEN PERFORMANCE IN MANY MINISTRIES.

19. (C) IT IS IMPORTANT TO NOTE THAT CHAVEZ IS IN THE PROCESS OF SHRINKING THE NUMBER OF MINISTRIES FROM 26 TO APPROXIMATELY 15, AND HAS DECIDED TO HOLD ALL MINISTRIES AND MINISTERS TO ACCOUNT. THIS HAS NOT BEEN DONE IN THE PAST. (HE ALSO HAS TO TACKLE THE PROMISED REDUCTION OF THE NUMBER OF GOVERNMENT EMPLOYEES, WHICH HE IS AVOIDING FOR THE TIME BEING.) IN THIS REGARD, CHAVEZ HAS INVITED SCRUTINY WHICH, WHILE IMPORTANT TO THE PROCESS OF CHANGE, WILL BE

PAINFUL FOR A NEW GOVERNMENT TRYING TO GET STARTED. IN SHORT, IT WILL TAKE A WHILE FOR THE NEW GOVERNMENT TO SETTLE IN.

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CONTINUITY OF ECONOMIC POLICY  
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¶10. (C) CHAVEZ'S CAMPAIGN RHETORIC HAD CREATED CONCERN WITHIN THE PRIVATE SECTOR THAT THE NEWLY-ELECTED PRESIDENT WOULD IMPLEMENT POPULIST ECONOMIC POLICY, DEEPENING VENEZUELA'S ALREADY SERIOUS ECONOMIC PROBLEMS. DURING HIS FIRST FIVE WEEKS IN OFFICE, HOWEVER, CHAVEZ HAS STEERED CLEAR OF SUCH POLICY, DECIDING INSTEAD TO MAINTAIN THE REFORM-MINDED ECONOMIC POLICY OF HIS PREDECESSOR. SPECIFICALLY, CHAVEZ HAS:

- NAMED MARITZA IZAGUIRRE AS FINANCE MINISTER (SHE WAS CALDERA'S FINANCE MINISTER AND THE GOV'S LINK TO THE MULTILATERAL BANKS);
- REQUESTED, IN THE ENABLING LAW HE SUBMITTED TO CONGRESS, EMERGENCY POWERS TO REINFORCE IZAGUIRRE'S APPROACH TO VENEZUELA'S FISCAL CRISIS THROUGH COST CUTTING AND REVENUE RAISING MEASURES;
- LEFT ANTONIO CASAS AS DIRECTOR OF THE CENTRAL BANK
- MAINTAINED CASAS' SCORCHED-EARTH DEFENSE OF THE STRONG BOLIVAR;
- BEGUN TALKS WITH THE IMF.

¶11. (C) CHAVEZ, COGNIZANT THAT HE DOES NOT HAVE THE ECONOMIC WHEREWITHAL TO MEET VENEZUELA'S PRESSING SOCIAL NEEDS, IS ATTEMPTING TO ENHANCE GOVERNMENT REVENUES. AGAIN, HE HAS FORSAKEN A POPULIST APPROACH. INSTEAD, HE HAS:

- REQUESTED AUTHORITY TO IMPOSE NEW TAXES, INCLUDING A VALUE ADDED TAX, FINANCIAL TRANSACTIONS TAX, AND REFORM OF THE INCOME TAX LAW;
- ORDERED IMPROVED TAX COLLECTION AT SENIAT AND CUSTOMS;
- LIMITED PUBLIC SECTOR WAGE INCREASES TO TWENTY PERCENT (BELOW THE 30 PERCENT INFLATION REGISTERED IN 1998, AND THE GOV'S LATEST PROJECTED INFLATION RATE OF 25 PERCENT IN 1999);
- AUTHORIZED THE STATE OIL COMPANY PDVSA TO BORROW USD 1 BILLION (WHICH MATCHES PDVSA'S ANTICIPATED ROYALTIES AND TAXES) ON THE INTERNATIONAL CAPITAL MARKETS;
- DECIDED TO FINANCE THE BS 800 BILLION DEFICIT FOR THE FIRST QUARTER OF 1999 THROUGH REDUCTION IN MONETARY STABILIZATION INSTRUMENT (TEMS) ISSUANCES AND AN EVEN GREATER EXPANSION IN ISSUANCE OF NATIONAL PUBLIC DEBT BONDS (DPNS).

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RACE AGAINST TIME  
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¶12. (C) CHAVEZ'S DECISION TO MAINTAIN CONTINUITY OF ECONOMIC POLICY IS DRIVEN BY THE PRIMACY OF HIS POLITICAL AGENDA. CONCERNED THAT DRAMATIC ENGAGEMENT WITH THE ECONOMY WOULD EXPOSE HIM TO POLITICAL ATTACK, CHAVEZ HAS DECIDED TO PUSH HIS POLITICAL AGENDA AS FAR AND AS FAST AS HE CAN BEFORE TURNING TO DEAL WITH THE ECONOMY. CONTINUITY OF ECONOMIC POLICY BUYS HIM SOME POLITICAL SPACE, SINCE THE CONSENSUS AROUND THIS POLICY ALREADY EXISTS.

¶13. (C) HOWEVER, CHAVEZ CAN ONLY CARRY THIS CONTINUITY FORWARD FOR SO LONG. HE KNOWS THAT HIS GOVERNMENT SITS ON A CRUMBLING ECONOMIC BASE. STILL DECLINING OIL PRICES AND SELF-IMPOSED PRODUCTION CUTS HAVE AGGRAVATED THE CURRENT RECESSION. HIGH INTEREST RATES AND THE INCREASINGLY OVERVALUED EXCHANGE RATE HAVE UNDERMINED THE HEALTH OF THE MANUFACTURING, AGRICULTURAL, AND TOURISM SECTORS. INFLATION IS STILL HIGH.

¶14. (C) ADDITIONALLY, CHAVEZ STILL HAS TO CONVINCE THE INTERNATIONAL FINANCIAL INSTITUTIONS (IFIS) AND THE FOREIGN BANKS THAT HE HAS THE POLITICAL AND ECONOMIC SITUATION IN HAND, AND THE POLITICAL WILL TO MAKE TOUGH DECISIONS. TO DO THIS HE NEEDS AN ARRANGEMENT WITH THE IMF AND PERSONAL EXPOSURE IN NEW YORK. CHAVEZ'S TWO POSTPONED VISITS HAVE HURT HIM, AND HE AND HIS TOP

ADVISORS ARE ONLY NOW UNDERSTANDING HOW MUCH.

¶15. (C) VENEZUELA'S BATTERED ECONOMIC AGENTS HAVE RESPONDED TO THESE WEAK ECONOMIC SIGNALS BY PREPARING FOR EVEN MORE DIFFICULT TIMES:

-- INVESTORS CONTINUE TO SIT ON THEIR WALLETS;

-- BANKS ARE PULLING BACK ON LOAN PORTFOLIOS AND INCREASING PROVISIONS FOR BAD DEBT;

-- COMPANIES ARE SHUTTING DOWN PLANTS AND ASSEMBLY LINES AND LAYING OFF WORKERS TO REDUCE COSTS;

-- WHOLESALERS AND RETAILERS ARE LOWERING PRICES TO CUT INVENTORIES;

-- CONSUMERS ARE FORGOING LUXURY ITEMS, POSTPONING LARGE PURCHASES, AND PAYING OFF CONSUMER DEBT.

¶16. (C) AS CHAVEZ ENTERS HIS SECOND MONTH OF GOVERNMENT, THE BIG QUESTION IS HOW LONG HE CAN POSTPONE MAJOR ECONOMIC REFORMS WHILE HE FULFILLS HIS POLITICAL AGENDA. THE REFERENDUM FOR THE HOLDING OF A CONSTITUENT ASSEMBLY IS SCHEDULED FOR APRIL 25. THE ELECTION OF THE ASSEMBLY, THE WRITING OF A NEW CONSTITUTION, A REFERENDUM TO ACCEPT THE NEW CONSTITUTION AND THE ELECTION OF A NEW CONGRESS WILL PROBABLY RUN THROUGH THE END OF THE YEAR.

¶17. (C) CHAVEZ'S EFFORTS TO MAINTAIN CONTINUITY OF ECONOMIC POLICY MAY NOT LAST THAT LONG. THE GOV HAS ENOUGH INTERNAL DOLLAR RESOURCES (THE REMAINING USD 680 MILLION IN TREASURY BONDS RELEASED FROM THE 1997 GLOBAL BOND SWAP AND USD 160 MILLION IN NON-MONETARIZED GOLD) TO MEET VENEZUELA'S FOREIGN DEBT PAYMENTS THROUGH THE END OF MARCH. AFTER THAT IT WILL HAVE TO RELY ON STATE OIL COMPANY PDVSA'S EFFORTS TO RAISE FUNDS IN THE INTERNATIONAL CAPITAL MARKETS AND THE CENTRAL BANK OF VENEZUELA'S DECLINING INTERNATIONAL RESERVES TO FINANCE FUTURE DEBT PAYMENTS. THE PDVSA BORROWING WILL BE COSTLY (300 TO 400 BASIS POINTS OVER TREASURY RATES) BECAUSE THE MARKETS KNOW THAT THESE FUNDS WILL END UP IN THE GOV'S ACCOUNTS. THE GOV WILL ALSO HAVE TO RELY ON THE ISSUANCE OF ADDITIONAL DPNS TO MEET THE GOVERNMENT PAYROLL. THIS QUIET SCRAMBLE FOR FOREIGN AND DOMESTIC RESOURCES SHOULD PAY THE GOV'S BILLS THROUGH THE END OF THE SECOND QUARTER.

¶18. (C) AFTER THAT, IT IS TOO DIFFICULT TO PREDICT. OIL PRICES MAY RECOVER, BUDGET CUTS AND REVENUE MEASURES MAY BEGIN TO TAKE EFFECT, AND THE GOV MAY BE ABLE TO MAKE IT TO THE END OF THE YEAR. ALTERNATIVELY, THE MARKET COULD LOOSE CONFIDENCE IN THE GOV'S ABILITY TO FINANCE ITS DEFICIT, PROVOKING A RUN ON THE BOLIVAR AND A SUDDEN LOSS OF RESERVES. THIS COULD FORCE THE GOV TO IMPLEMENT PRICE AND EXCHANGE CONTROLS OR A MAXI-DEVALUATION. THE RESULTING SURGE IN INFLATION COULD THEN UNDERMINE CHAVEZ' POLITICAL SUPPORT AND INVIGORATE HIS POLITICAL OPPOSITION IN THE MIDST OF THE POLITICAL REFORM PROCESS.

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WHAT IT ALL MEANS  
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¶19. (C) CHAVEZ WAS ELECTED TO BRING ABOUT SIGNIFICANT POLITICAL CHANGE IN VENEZUELA. IT IS UP TO HIS GOVERNMENT, THROUGH CONSTITUTIONAL CHANGE, IMPROVED GOVERNMENT, AND ECONOMIC REFORM, TO MAKE DEMOCRACY AND ITS INSTITUTIONS MEANINGFUL TO THE EVERYDAY CONCERNS OF VENEZUELAN. HE UNDERSTANDS THAT HE IS THE CONSEQUENCE, AND NOT THE CAUSE, OF CHANGE IN VENEZUELA.

¶20. (C) HE ALSO UNDERSTANDS THAT HIS POLITICAL AGENDA IS MOVING THROUGH A NARROWING ECONOMIC SPACE. HE MIGHT NOT BE ABLE TO COMPLETE HIS IMMEDIATE POLITICAL AGENDA BEFORE HE IS CAUGHT IN AN ECONOMY IN DEEP CRISIS. HOWEVER, HE INTENDS TO GET AS FAR ALONG THE PATH OF POLITICAL CHANGE AS POSSIBLE. AT THE LEAST, HE HOPES TO HAVE A CONSTITUTIONAL ASSEMBLY IN PLACE THAT SUPPORTS HIS POLITICAL AGENDA.

¶21. (C) CHAVEZ'S FIRST FIVE WEEKS IN OFFICE HAVE BEEN DRAMATIC AND HIGHLY-CHARGED. NO VENEZUELAN PRESIDENT HAS BROUGHT SUCH EXPECTATION TO OFFICE. NO VENEZUELAN PRESIDENT HAS SET SUCH A HIGH STANDARD FOR HIMSELF AND HIS ADMINISTRATION. NO VENEZUELAN

PRESIDENT HAS EVER ANTICIPATED SUCH DIRE RESULTS SHOULD HE FAIL. GIVEN THIS, CHAVEZ'S IS OFF TO A DECENT START. HOWEVER, TO SUCCEED, CHAVEZ MUST USE THE NEXT MONTHS TO MAINTAIN THE MOMENTUM OF HIS POLITICAL AGENDA, IMPROVE HIS ADMINISTRATION, AND HOPE THE ECONOMY CONTINUES TO HOLD TOGETHER AS HIS INHERITED REFORMIST ECONOMIC POLICY, WITH HELP FROM THE IFIS AND FOREIGN BANKS, FALLS INTO PLACE. THIS IS A TALL ORDER, BUT ONE THAT HE APPEARS TO BE DOGGEDLY COMMITTED TO CARRY THROUGH.

MAISTO